

# TheMarker

## Erel Margalit – the Venture Capitalist with the Golden Touch

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**Who is the best venture capitalist of the past decade? According to *The Marker*, Erel Margalit, founder of Jerusalem-based venture capital fund JVP, is the fund manager with the greatest number of exits to his credit during the last decade - seven, to be exact.**

**Ranked second - four fund managers with four exits each: Ruti Alon of Pitango Venture Capital, Haim Sadger of Sequoia Capital Israel, Yoram Oron of Vertex Venture Capital and Yossi Sela of Gemini Israel Funds. In third place – five managers: Shlomo Dovrat of Carmel Ventures, Boaz Dinte of Evergreen Venture Partners, Rami Bracha of Pitango Venture Capital, Hadar Ron of Israel Health Care Ventures and Eddie Shalev of Genesis Partners.**

Margalit is credited with seven exits in the last decade. He invested in Precise Software Solutions, which was sold to Veritas Software for \$537 million; Sheer Networks, which was sold to Cisco for \$100 million; Allot, which went public on NASDAQ; Cogent Communications, which went public on NASDAQ; Viryanet, which went public and was later sold to a private fund and Paradigm Geophysical, which was sold as well.

The board of directors' job in a startup company is slightly different than that of boards in larger and more mature companies. Board of directors of budding

technology companies have a significant role in creating the opportunity for the company to take off and produce a return on investment in the future.

Boards usually consist of two, often opposing, forces. On the one hand are the founders, who usually regard the company as their precious "baby", whereas the venture capital board members, who have invested in the company, will usually do everything in their power to steer the company towards profitability or, at least, financial stability.

### **The Director in the role of "the Responsible Adult"**

A good director can lift up a company and a bad one can ruin it. When a venture capital fund invests in a company, it receives a seat in the company's board. This is not just a formal role. The fund has a vested interest in the partner--director becoming acquainted with the company and its area of activity and in enabling it to grow. This is exactly where the expression "smart money" vs. "stupid money" comes into play. The fund helps the entrepreneur by infusing the company with capital, but it also provides him with knowledge that will help increase the company's value. Venture capitalist board members assist the company and contribute from their vast knowledge to the young company. As the "responsible adult" they focus the entrepreneurs, who are usually technology-driven, on business goals.

Yigal Rotem, founder of PowerDsine, which was sold to Microsemi for \$542 million, tries to explain what goes on in board meetings. "Meetings take place on a regular basis, once a quarter. They are very structured. The first part consists of a business review. The second part deals with the more administrative side and with approving decisions, such as approving budgets or appointment of key personnel."

Have you ever been angry at board members who were not active enough on behalf of the company?

"I never felt angry at them. The role of board members is not to run the company. Their role is to help the company, to act as an advisory, thinking organ. Every

high tech company goes through different stages during its lifecycle. When the company is young, the entrepreneurs are less experienced and need more hands-on assistance. They also need assistance in raising capital and laying a proper financial infrastructure, and ongoing support in building the organizational infrastructure.

“As the company matures, assistance would need to focus on guidance and advice on marketing and sales: where does it make most sense to open up an office? Who should be hired? Thinking is much more strategic and long-term. They also help with locating strategic partners and putting together the business investment portfolio. A board of directors need not operate in a hostile way and board members do not necessarily need to terrorize the CEO.”



Have you ever left a board meeting feeling it was a waste of time?

“There are meetings where you emerge with insights and there are meetings where all you accomplish is approving a budget or the opening of an office somewhere in the world. A good board of directors can contribute to the company and upgrade it by 10%-20%, but a bad board can kill a company. I know quite a few companies like that. This can happen when management is replaced in an unpleasant manner or when management is constantly in disagreement with members of the board. In such cases, if management is not replaced on time, the company will continue to deteriorate and will pass the point of no return.”

“Good members of the board can greatly influence a company’s lifecycle and help it achieve an exit. Board members often need to rescue the company from

problematic situations,” says Erel Margalit, founder of JVP venture capital fund, who is credited with seven major exits in the past decade (see box). “Take Cogent Communications, for example, which we founded at the height of the telecom bubble, in early 2000. Almost all similar companies closed down. I worked in close coordination with the CEO through some difficult moments, when other funds wanted out and to discontinue financing the company. When there is a crisis the question is what to do next. Do you sell the company early? Do you continue to support it? How does one solve problems which arise vis a vis other fund managers who have lost faith in the company? My job is to put my ego aside and see what is bothering each and every director from other funds that have invested in the company.

“Sometimes you have to acknowledge the fact that it’s a weak or mediocre company, and you need to steer it to safety, to a modest exit or a merger. Sometimes you need to explain to a CEO why he cannot shoot himself in the foot when he plans, for example, to raise money at an insane value.

“There are many good directors in the Israeli venture fund arena, but if I examine what has guided me throughout the years, it is the following pattern: support the CEO or management even when the market doesn’t support the company; make difficult decisions and make changes if something is not working properly; and continue to support the company and give it enough breathing room to make as much progress as possible. When a company is in a good state, it receives quite a few acquisition propositions. It wants to complete that episode successfully. But when a company is truly promising and a leader, it shouldn’t be afraid of conquering the market.

“The greatest fear is not of failure but of success. I’ve already been in several situations where a company wants to be sold. The CEO would tell me that the employees are looking for security and that he, too, is interested in completing an exit and getting sold. I told him that the guys who came to work for him did not come because of the security he provides them, but because of the dream he offers them.”

## **”There is no such thing as a Non-Destructive Board of Directors”**

Adi Pundak-Mintz, managing partner at Gemini Israel Funds, believes that some of the directors at VC-funded startups in Israel are simply not good enough. Pundak-Mintz took two companies to exits of over \$100 million – Traiana, which was sold to ICap for \$247 million, and Diligent Technologies, which was sold to IBM for \$165 million.

“I don’t think companies succeed due to the influence of a director. The role of the director is to support the CEO and help him see things he might have missed, but at the end of the day, a director provides a service.”

Can a director from a venture fund ruin a company and not just cause it to succeed?

“There is no doubt that this happens. There is no such thing as a non-destructive board of directors. When I first arrived at Gemini, I was taught a line from the Hippocratic Oath: ‘Do no harm’. The odds of a director doing harm to a company are very high, especially if he does not understand the market and is dogmatic.”

You are familiar with quite a few [Israeli] board of directors of startup companies. How good are they?

“Some don’t want to make an effort. Others come to meetings unprepared. I believe 50% of [Israeli] VC directors are that way.”

Dov Moran, founder and CEO of Modu, believes the board of directors has a very significant role in companies. “The board needs to serve as an outer eye for the CEO that helps him see the right way. Good directors are very involved, hand out advice, give support, and if the CEO is not good – replace him and appoint a substitute. The problem is that in many instances, directors become confused, thinking their job is to run the company or run the CEO. In many cases they don’t have the experience that truly enables them to become mentors to the CEO. And, of course, there are many cases where directors come to the quarterly meeting to sip coffee and devour burekas.”

Moran extends a piece of advice to entrepreneurs: “If it’s in your power, build a good board of directors with people you get along with, people who have been managers and have experienced what you are about to experience. Get their advice formally and informally. And don’t forget for a minute that the board represents your investors and is therefore, in effect, your boss.”

### **“Directors Outline the Right Strategy”**

Ruti Alon, managing partner at Pitango Venture Capital, on the other hand, believes that good directors have great influence on the manner in which a company moves forward. “Many companies lack a correct strategy,” says Alon, who specializes in supporting life science companies.

“One of the director’s roles is to outline a strategy which will lead to growth and success. The second role is to assist in recruiting senior employees. And the third thing a director can help with is in global networking. A good director needs to examine whether the company is working according to plan and according to budget and whether it is succeeding or not. If it isn’t – why not, and what can be done to correct and improve things?”

From what you’ve seen, do Israeli directors make the effort and prepare for meetings?

“Most do their homework, since I believe the director’s role involves a great deal of responsibility. And if someone comes just for decoration, he is of no use. In startup companies that I am involved with, people take things seriously. You want to get to where the board of directors includes members who have different abilities. Where one is more versed in finances and another – in technological aspects. A board of directors needs to be diversified.”

### **“A Director Should Support the CEO”**

Shlomo Kalish, founder of Jerusalem Global Ventures, who was ranked 39th on the Forbes Midas List due to such investments as Saifun Semiconductors and

PowerDine he made when he was still a partner at Concord Ventures, says the role of a good board member is to support the CEO, since the latter is a very lonely person. "A CEO cannot consult the people under him since he needs to act as their leader. On the other hand, he has no boss. That is why he is lonely.

"A good board member needs to be as available and supportive as possible to the CEO. A bad board member will try to run the CEO.

"There are cases where managing partners who serve as board members were themselves CEOs in the past, so there is a danger that they may try and interfere with the decisions of the CEO. I've seen cases where a bad board of directors caused a company to become dysfunctional."

Can a director prepare a company for exit?

"My belief is you don't prepare a company for exit, you build a company so that it becomes successful. But when an exit takes place, it is very important that a director involved in the process has experience, because the game needs to be played well. If you don't have a good director who is experienced in mergers and acquisitions, you are better off hiring a good investment banker.

"I have already experienced situations where a company was sold for three times the original offer. This may mean a lot of money, and you can't make mistakes."

You have supported quite a few companies and currently serve on the board of five. What is your message to entrepreneurs?

"Just as the investor conducts due diligence of the entrepreneur before investing in him, the entrepreneur needs to examine his directors."

**\*\*\*How did we conduct our assessment?**

We arrived at the result in the following manner: We examined all exits accomplished from 2001 to 2009. An exit was defined as a sale or a merger of a company at a value of at least \$100 million. We also included in the list IPOs in excess of \$100 million. Our purpose: to identify the most successful venture

capital managing partners, and to attempt to learn from them management practices used to lead their companies to success.

A disclaimer is in order: First, a director's contribution to a company represents only one variable in the success formula. An entrepreneurial team, promising technology, luck and timing are no less important; secondly, there are many good directors who have done well with their portfolio companies and have achieved exits with excellent multipliers, even greater than those with nine-digit exits, but their price tags were under \$100 million.

### List of Venture Capital Partners Exits In Israel in the Past Decade (more than \$100 million)

Name of partner	Number of exits	The companies	Fund
Erel Maragalit	7	Precise Software Solutions, Sheer Networks, Allot, Cogent Communications, Netro Corporation, Viryanet & Paradigm Interactive.	JVP
Yossi Sela	4	Precise Software Solutions, Veracity Technologies, Saifun Semiconductors & Allot	Gemini Israel Funds
Haim Sadger	4	Traiana, Jajah, Followap Telecommunications, Actona Technologies	Sequoia Capital Israel
Yoram Oron	4	Scopus Video Networks, Actimize, PowerDsine, Voltaire	Vertex Venture Capital
Ruti Alon	4	Ventor Technologies, Colbar LifeScience, Disc-O-Tech Medical Technologies, Optonol Ltd.	Pitango Venture Capital
Shlomo Dovrat	3	Coppergate, Followap Telecommunications, ECI Telecom	Carmel Ventures
Rami Bracha	3	Dune Networks, Gteko Ltd., Radlan	Pitango Venture Capital
Hadar Ron	3	Optonol Ltd., Colbar LifeScience & Syneron Medical Ltd.	Israel Health Care Ventures
Eddie Shalev	3	Kidaro, Optonol Ltd., Colbar LifeScience	Genesis Partners
Boaz Dinte	3	Dune Networks, BigBand Networks, P-Cube	Evergreen Venture Partners

